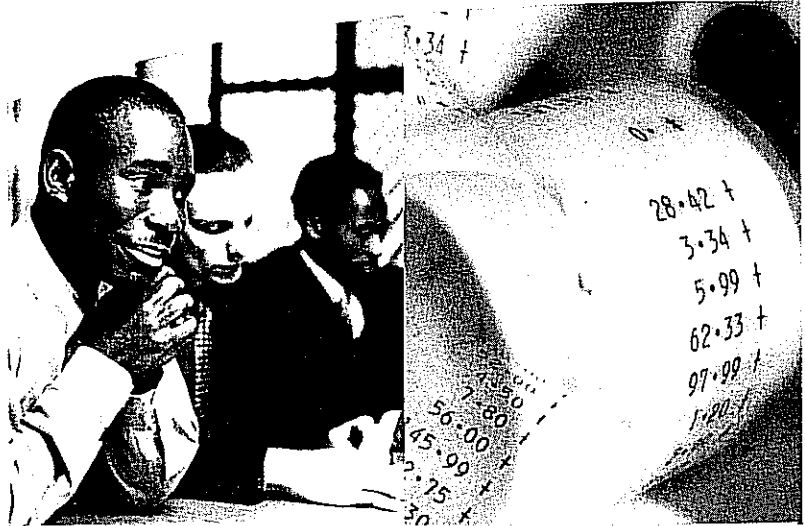




AUDITOR - GENERAL



**REPORT OF THE AUDITOR-GENERAL
TO THE
NORTHERN CAPE
PROVINCIAL LEGISLATURE
ON THE FINANCIAL STATEMENTS AND
PERFORMANCE INFORMATION OF
KHÂI- MA MUNICIPALITY
FOR THE YEAR ENDED
30 JUNE 2008**

Accountability

Integrity

Independence

**REPORT OF THE AUDITOR-GENERAL TO THE NORTHERN CAPE PROVINCIAL
LEGISLATURE AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND
PERFORMANCE INFORMATION OF THE KHÂI-MA LOCAL MUNICIPALITY FOR
THE YEAR ENDED 30 JUNE 2008**

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Khâi-Ma Local Municipality (municipality) which comprise the statement of financial position as at 30 June 2008, statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on page 8.

Responsibility of the accounting officer for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting determined by the National Treasury, as set out in accounting policy note 1 and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2007 (Act No. 1 of 2007) (DoRA). This responsibility includes:
 - designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
 - selecting and applying appropriate accounting policies
 - making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing and *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance on whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but

not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

6. An audit also includes evaluating the:
 - appropriateness of accounting policies used
 - reasonableness of accounting estimates made by management
 - overall presentation of the financial statements.
7. Paragraph 11 *et seq.* of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.
8. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis of accounting

9. The municipality's policy is to prepare financial statements on the basis of accounting determined by the National Treasury, as set out in accounting policy note 1.

Basis for qualified opinion

Provisions

Leave provision

10. The integrity of the data maintained on the Tribal system (personnel system) was tested, to determine whether the leave data maintained thereon can be relied upon. During the aforementioned testing it was noted that a large number of leave forms (leave taken) had not been recorded on the personnel system, rendering the leave data incomplete. Due to the unavailability of information and supporting documents, alternative procedures could not be performed to resolve the limitation of scope imposed by the incomplete leave system. As a result, I could not express an opinion on the completeness, rights and obligation, and valuation of the provision for leave pay.

Provision for doubtful debts

11. Good financial management discipline requires management to assess the recoverability of debtors and make adequate provision for irrecoverable debtors. Debtors amounted to approximately R6,6 million at year-end (2006: R4,7 million), before taking into account any provision for doubtful debts.

Debtors outstanding for longer than 90 days amounted to R6 078 444. The recoverability of these debtors is doubtful, as a major portion of this amount is due by indigents. The current provision for bad debts amounts to R171 240. The provision has been understated by R5 907 204 in the annual financial statements. As a result, the provision for bad debts is neither complete nor fairly valued.

Provision for the rehabilitation of the land refill site

12. No provision was made in the financial statements for the rehabilitation of the land refill site. The effect in the financial statements could not be verified, as the volume of the current site could not be submitted for audit purposes. Accordingly, I could not satisfy myself as to the existence, valuation, rights and obligation, and completeness of provisions.

Provision for post-retirement medical obligations

13. No provision was made in the financial statements for post-retirement medical obligations. The effect in the financial statements could not be verified, as no documentation regarding post-retirement medical obligations could be submitted for audit purposes. Accordingly, I could not satisfy myself as to the existence, valuation, rights and obligation, and completeness of provisions.

Property, plant and equipment

14. None of the fixed assets were uniquely numbered, resulting in movable assets to the amount of R28 222 487 not being easily identifiable; i.e. the fixed assets could not be traced from the physical assets to the fixed asset register and from the fixed asset register to the physical assets. Accordingly, I could not satisfy myself as to the existence of fixed assets.
15. The tender agreement for the erecting of the 15-metre-high mast lighting to the value of R468 444 could not be submitted for audit purposes. Accordingly, I could not satisfy myself as to the existence, valuation, rights and obligation, and completeness of mast lightings included in fixed assets.

Going concern

16. The municipality's financial statements have been prepared on the going concern basis, which assumes that the municipality will be able to meet its future obligations and commitments in the ordinary course of business. Accordingly, these financial statements do not include any adjustments relating to the valuation of assets and the classification of liabilities, which might be necessary if the municipality is unable to continue as a going concern.

Without the continued support from national and provincial government, it is evident that the municipality will not be able to fulfil all its current and long-term obligations. The following conditions indicated the existence of a material uncertainty that may cast significant doubt on the municipality's ability to continue as a going concern:

- **Increase in debtors**

The debtors' turnover in days was calculated at 259 days (2007: 194 days), indicating a deterioration year on year. Long-outstanding debtors (91 to 365 plus days) represented 85,70% of total debtors disclosed in the financial statements.

- **Increase in bank overdraft**

The bank account was in overdraft for a large part of the year, which is in contravention of section 10(G)(8)(a)(ii) of the Local Government Transition Act, 1993 (Act No. 209 of 1993) (LGTA). The overdraft of the municipality increased by 36% from R563 331 (2006) to R768 756 (2008). This was also an indication that the municipality experienced cash flow problems during the financial year under review. The bank overdraft was exceeded by R68 756.

Employee costs

17. During the audit, management could not provide the employee files for all new appointments made during the year. Due to a lack of information and supporting documentation, posing a limitation of scope, alternative procedures could not be performed to verify the occurrence, accuracy and classification of employee costs. As a result, I do not express an opinion on the occurrence, accuracy and classification of employee costs.

Disclosure

18. Adequate information regarding the credit risk and cash flow interest rate risk of financial liabilities and financial assets, as required by International Accounting Standard 32, was not disclosed in the financial statements. This resulted in the incomplete disclosure and presentation of the annual financial statements.

Qualified opinion

19. In my opinion, except for the effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Khâi-Ma Local Municipality as at 30 June 2008 and its financial performance and cash flows for the year then ended, in accordance with the basis of accounting as determined by the National Treasury, as set out in accounting policy note 1 and in the manner required by the MFMA and DoRA.

Emphasis of matters

I draw attention to the following matters:

Unauthorised expenditure

20. As disclosed in note 36.1 to the financial statements, unauthorised expenditure amounting to R880 000 was incurred during the financial year, as conditional grants were used to finance some of the operating activities of the municipality.

Amendments to the applicable basis of accounting

21. As set out in accounting policy note 1, the National Treasury approved a deviation from the basis of accounting applicable to the municipality in terms of *General Notice 552 of 2007*, issued in *Government Gazette No. 30013 of 29 June 2007*.

OTHER MATTERS

I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

Internal controls

22. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the inefficiencies in the system of internal control, which led to the qualified opinion. The root causes are categorised according to the five components of an effective system of internal

control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Risk assessment	Control activities	Information and communication	Monitoring
Leave pay provision	X				
Provision for doubtful debts	X				x
Property, plant and equipment	X		X		X
Provision for the rehabilitation of the land refill site	X			X	X
Tender agreements not submitted for audit purposes	X		X		X
Provision for post-retirement medical obligations	X		X		X
Going concern	X		X		X
Documentation not submitted for audit purposes	X		X		X
Disclosure	X		X		X
<u>Control environment</u>: establishes the foundation for the internal control system by providing fundamental discipline and structure for financial reporting. <u>Risk assessment</u>: involves the identification and analysis by management of relevant financial reporting risks to achieve predetermined financial reporting objectives. <u>Control activities</u>: policies, procedures and practices that ensure that management's financial reporting objectives are achieved and financial reporting risk mitigation strategies are carried out. <u>Information and communication</u>: supports all other control components by communicating control responsibilities for financial reporting to employees and by providing financial reporting information in a form and time frame that allows people to carry out their financial reporting duties. <u>Monitoring</u>: covers external oversight of internal controls over financial reporting by management or other parties outside the process; or the application of independent methodologies, like customised procedures or standard checklists, by employees within a process.					

Non-compliance with applicable legislation

Municipal Finance Management Act, 2003 (Act No. 56 of 2003)

23. Evidence that the accounting officer had informed the National Treasury of the overdrawn bank accounts of the municipality could not be submitted for audit purposes, as prescribed by section 70(2) of the MFMA.
24. The responsibilities of different levels of management and their roles in decision-making were not approved, documented and communicated to all staff in the municipality, as prescribed by section 79 of the MFMA.
25. A statement in the prescribed format on the state of the municipality's budget was not submitted to the provincial treasury within 10 working days after the end of each month, as prescribed by section 71(1) of the MFMA.
26. Policies were in place with regard to some activities of the municipality, but not for all main categories, as stipulated by section 65(2)(a) – (h) of the MFMA.
27. The municipality did not have a fraud prevention plan to prevent and detect fraud and to mitigate specific fraud risks, as prescribed by section 115(1)(b) of the MFMA.
28. Evidence could not be submitted for audit purposes that reports regarding unauthorised, irregular and wasteful expenditure incurred by the municipality had been submitted to the MEC for Local Government and the Auditor-General, as prescribed by section 32(4) of the MFMA.
29. Creditors' reconciliations were not performed by the municipality, as stipulated by section 65(2)(j) of the MFMA.
30. The municipality did not adhere to section 115(1)(b) of the MFMA, as the accounting officer did not take all reasonable steps to ensure that proper mechanisms and separation of duties in the supply chain management system were in place to minimise the likelihood of fraud, corruption, favouritism, and unfair and irregular practices.
31. Suppliers were not paid within 30 days of receiving the relevant invoice, as stipulated by section 65(2)(e) of the MFMA.
32. Evidence could not be submitted for audit purposes that the mid-year assessment performed by the municipal manager had been submitted to the National Treasury and the provincial treasury, as prescribed by section 72 of the MFMA.
33. Evidence could not be submitted for audit purposes that reports on the functioning of the supply chain management function of the municipality had been submitted to the National Treasury and the provincial treasury as well as the Auditor-General, as prescribed by section 114 of the MFMA.

Municipal Systems Act, 2000 (Act No. 32 of 2000)

34. Monthly expenditure reports were not made public, as stipulated by section 21A of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).
35. Documented evidence could not be obtained of alterations made to the remuneration packages of the senior management of the municipality, as prescribed by section 60(1) of the MSA.

Supply chain management regulations

36. The municipality did not obtain tax clearance certificates from suppliers to whom awards above R15 000 were made during the year, as prescribed by regulation 43 of the supply chain management regulations.

Matters of governance

37. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of certain key governance responsibilities, which I have assessed as follows:

Matter of governance	Yes	No
Audit committee		
• The municipality had an audit committee in operation throughout the financial year.		✓
• The audit committee operates in accordance with approved, written terms of reference.		✓
• The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.		✓
Internal audit		
• The municipality had an internal audit function in operation throughout the financial year.	✓	
• The internal audit function operates in terms of an approved internal audit plan.		✓
• The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.		✓
Other matters of governance		
• The annual financial statements were submitted for audit as per the legislated deadlines in section 126 of the MFMA.	✓	
• The annual report was submitted to the auditor for consideration prior to the date of the auditor's report.		✓
• The financial statements submitted for audit were not subject to any material amendments resulting from the audit.		✓
• No significant difficulties were experienced during the audit concerning delays or the unavailability of expected information and/or the unavailability of senior management.		✓
• The prior year's external audit recommendations have been substantially implemented.		✓
Implementation of Standards of Generally Recognised Accounting Practice (GRAP)		
• The municipality submitted an implementation plan, detailing progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 30 October 2007.	✓	
• The municipality substantially complied with the implementation plan it submitted to the National Treasury and the relevant provincial treasury before 30 October 2007, detailing its progress towards full compliance with GRAP.	✓	
• The municipality submitted an implementation plan, detailing further progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 31 March 2008.	✓	

Unaudited supplementary schedules

38. The supplementary information set out on pages 43 to 44 does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion on them.

OTHER REPORTING RESPONSIBILITIES

REPORTING ON PERFORMANCE INFORMATION

39. I was engaged to audit the performance information.

Responsibility of the accounting officer for the performance information

40. In terms of section 121(3)(c) of MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the MSA.

Responsibility of the Auditor-General

41. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate audit evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
42. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Responsibility of the Accounting Officer

Audit findings (performance information)

Non-compliance with regulatory requirements

43. The annual report of the municipality did not include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the MSA, as required by section 121(3)(c) of the MFMA.
44. The municipality did not, within the prescribed period after the start of its elected term, adopt a single, inclusive and strategic plan for the development of the municipality, as required by section 25 of the MSA.

OTHER REPORTS

Investigations in progress or completed

45. There is a possibility of fraud relating to monies amounting to R14 273 received in respect of NaTIS. The matter is still under investigation by the municipality.
46. Monies amounting to R4 379 were stolen from the cash office. The matter is still under investigation.

APPRECIATION

47. The assistance rendered by the staff of the municipality during the audit is sincerely appreciated.

Auditor-General

Kimberley

27 January 2009



AUDITOR-GENERAL